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## Industry Trends for 2018

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**Agents, product executives and other experts from around the F&I industry share their hopes, fears and predictions for the auto finance market in the year ahead.**

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After a transformative year for the automotive industry, the economy, politics, sports and entertainment, it's difficult to imagine what 2018 might have in store. To get a sense of what the new year could bring for your agency, your dealer clients and their customers, *Agent Entrepreneurs* sought opinions and prognostications from 23 of the F&I industry's leading executives and experts.



Their collective outlook, though largely positive, may surprise you, and should leave no doubt that further, sweeping changes lie ahead.

### **The Economy**

U.S. economic indicators are encouraging. New-vehicle sales have plateaued — but not plummeted — following the record-high 17.5 million units sold in 2016 and the record-high seasonally adjusted annual rate (SAAR) of 18.4 million set in November 2015. The stage is set for continued prosperity in 2018.

“It's good news pretty much all around for the economy as a whole,” said Jeremy Lindsey, COO of Alpha Warranty Services. “Experts are predicting U.S. GDP growth to come in around 2.5% in 2018, which is up from a projected 2.2% increase in 2017 and only 1.6% in 2016. That's very good news for the U.S. economy, which has seen an uptick in consumer spending and private investments in businesses in 2017. Consumer spending represents around 70% of GDP, so it's a crucial indicator of economic health.”

Lindsey predicted the Federal Reserve will be “more active” in 2018, pursuing further incremental increases in interest rates as the economy continues to expand and low unemployment drives wages up. He also expects franchised and independent dealers to compete more intensely for used units as new-vehicle sales decline, citing a National Automobile Dealers Association (NADA) forecast that new-car dealers alone will sell 15.3 million pre-owned cars and trucks in 2018, up from 15.1 million last year.

Brent Griggs, president and CEO of Portfolio, predicted continued slow economic growth “with no major disruptions” in 2018. “Interest rates will remain at their historically low levels but will continue to inch

upward with inflation. I expect new auto sales to decline 2% to 3% for the second straight year but used-car sales to increase by a like amount due to falling prices and increasing supply.”

“The tailwinds of improved light-vehicle sales — potential tax breaks, continued low interest rates, cheap gasoline and stable availability of credit will likely be offset by the headwinds — pent-up demand spent, decrease in demand for passenger-car models, waning of OEMs’ appetites for incentive spending, ridesharing, and the sales bump caused by 2017 hurricanes exhausted,” said Bob Pruitt, president of Cal-Tex Protective Coatings, who predicts new-vehicle sales to finish at or near 16.7 million units. “The positive spin is that dealers should be motivated to increase PRU through F&I products to compensate for lower vehicle counts.”

Randy Crisorio, president and CEO of United Development Systems Inc. (UDS), suggested a similar estimate for new-car sales in an economy that has “a lot of momentum” going into the new year.

“As I take note of my thoughts, the stock market is raging, new construction seems to be everywhere, and the tax plan appears to be close to confirmation,” Crisorio said. “The White House continues to remove regulatory roadblocks that stand in the way of business, no matter the size, and American ingenuity is finding a variety of ways to maintain the energy in new-vehicle sales. Taking it all in, the economic outlook for 2018 is very positive. I believe that new-year vehicle sales will be much in the image of 2017, continuing the good run.”

Larry Dorfman took a less rosy view, blaming “confusion and divisiveness in Washington” for a lack of progress on such significant issues as health-care reform and, until Dec. 22, tax reform.

“I’m really not sure any more will get done in 2018 than this administration got done in 2017. ... By the time this article comes out, we will know if the tax bill has passed and, if it does, with the provisions in it as I write this we will have damaged income earners who make under \$70,000 annually, caused millions of people to be without health care, significantly increased the cost of health care for those who can get it, and increased our budget deficit by \$1 trillion or so,” said Dorfman, who serves as chairman of APCO Holdings, home of the EasyCare and GWC Warranty brands. “If that is the case, I believe we will see a significant drop in the economy over the next few years. Otherwise, I see a flat to down market with a SAAR of around 16.6 million or so and increased used-vehicle sales.”

Rick Knight, the founder and president of Performance Admin Corp., is counting on the steadily declining U.S. unemployment rate — in combination with an ever-growing population — to create new customers throughout the year.

“Over the last 10 years, the number of licensed drivers in the U.S. has grown from 190 million to over 218 million. This will create more opportunity for new and pre-owned vehicle sales, since most Americans rely on their vehicle as the means of transportation to their job,” Knight said.

“I see a strong economy for 2018, especially if tax reform is passed,” said Jeff Wanning, senior vice president at Central States of Omaha (CSO). “If the Fed ticks up interest rates, it could have a negative impact on the cost of borrowing money. However, I don’t foresee an increase significant enough to

dramatically affect car loans. Most analysts are predicting the SAAR to be in the 16.5-million range, which is only a slight decrease from 2017 projections.”

Daniel Lievrouw, senior vice president and CIO of American Guardian Warranty Services (AGWS), predicted a growing economy and a “close to flat” auto sector. “Some of this, I believe, is due to the longer finance terms keeping buyers from getting into an equity position as quickly as they used to, combined with continuing lease penetration. We will see how tax reform ends, but without backdating these changes into 2017, it will take some time for most households to really see the benefit that should be coming.”

“The economy is going well, by most measures. We rightfully will continue to worry about something geopolitical that can turn this momentum in the wrong direction,” said Dave Duncan, president of Safe-Guard Products, noting that 17 million new-car sales is “definitely not a bad place to catch your breath. ... I still maintain that we go higher from here, but maybe not in 2018. We predicted a flat SAAR when we built out our budget models for 2018. Meanwhile, used cars is the place to make your hay next year. Lots of inventory, plenty of credit and ways to manage the clumsy logistical side of used cars like never before.”

“There are puts and takes across the economic landscape — interest rates rising, credit tightening, low unemployment, tax cuts, etc. — but, overall, we are expecting sales to be flat in 2018 compared to 2017,” said Patrick Brown, CEO of Innovative Aftermarket Systems (IAS). “But the economy is on solid footing, and in general, that is a good sign for the entire industry.”

## **The Industry**

Pivoting from the U.S. economy as a whole to the finance and insurance industry in particular, Jimmy Atkinson points to a number of “high-level” issues that will affect F&I product sales in 2018 and beyond.

“Tesla and its push to bypass franchise laws and sell direct is one. The impact a tax change may have and the overall shift in the regulatory environment is another,” said Atkinson, who serves as president and CEO of AUL Corp. “While the relaxing of federal oversight is welcomed, as an industry, my belief is we need to keep pushing for transparency in how we present, price and fulfill our products.”

“Consumers are demanding that we don’t just ‘sell them products’ but rather provide full solutions that solve their problems and address their needs,” said Brian Krasavage, vice president of Allstate Dealer Services. “With that as the backdrop, we are focused on providing more innovative F&I product solutions that are easier for dealers to deliver and sell and for consumers to purchase, own and utilize.

“The good news is that, if we as an industry can deliver against these expectations, I believe there will be an opportunity for increased penetration and sales. I expect we’ll see quite a bit of new capabilities and experimentation in this area in 2018,” Krasavage added, noting that consumers’ appetite for more information about F&I “earlier in the buying process” will continue to grow in 2018. “They expect the purchase experience to be more seamless and simple and want to know exactly what they are buying and what their coverage is if they have to make a claim.”

Cindy Allen, the new CEO of StoneEagle, expects F&I production to slowly trend downward along with sales. And there's more bad news for agents and dealers, particularly those who rely solely on products for new-car buyers. She expects leasing and direct-to-consumer sales to continue to increase in 2018. However, she noted, "It appears that direct-to-consumer providers still have a long way to go in understanding how to sell F&I in the online purchase process. Many technology companies are trying to solve the online rating and purchasing challenge."

Allen also shared her concerns about GAP, noting that a host of factors, including a devastating Atlantic hurricane season that resulted in "massive claims," has driven losses to shocking heights. "These claims will certainly cause an actuarial 'reset' of GAP premiums. Our concern is that rate increases could turn GAP into a product that is less viable and has less profit in the F&I office and reinsurance programs."

GAP pricing will be a "big issue" in 2018, Dorfman said. "The losses being incurred across the industry now are just the beginning. As pre-owned vehicle values drop, those losses will get bigger and rates will be going up consistently. At the same time, GAP is still a huge value for customers, and I believe it will be an important purchase in F&I. Its value is certainly well-established at this point."

"The continuing stress that is on GAP reserves and the inevitable increases in pricing will move GAP down the menu," said Cal-Tex's Pruitt. "Non-cancelable ancillary products will move up the menu. ... Another factor that will continue to impact the industry is the rising costs of replacement parts. Technological advances in vehicles have increased the costs to replace the vehicle's parts, such as head-up displays on windshields."

On the flip side, said Jennifer Holcomb, autonomous vehicle technology is a "huge trend" that could ultimately reduce losses thanks to the elimination of human error.

"I've noticed autonomous cars in cities like Tempe recently, and it's interesting to see where that sector is heading and how it will affect aftermarket product sales," said Holcomb, vice president of operations for Classic Products/Norman & Co. However, she noted, "Autonomous vehicles have even more expensive electronic equipment, so how will that affect vehicle service contracts and GAP claims?"

"We will continue to watch the ever-growing impact from ridesharing and the strong push from manufacturers for both autonomous vehicles and electric vehicles," said IAS's Brown. "As an industry, it's important to develop product offerings and underwriting strategies for these emerging trends."

"The two most immediate trends to monitor in 2018 are the continued push to move F&I online and the home delivery sales model being pioneered by Carvana, an online-only used-car dealer that lets customers shop, finance and trade cars through its website," said Robert Steenbergh, CEO of US Equity Advantage. "Personally, I would never purchase a car that way, but I'm very interested to see if there is a significant demographic that will."

UDS's Crisorio said industry members must be "nimble" to adequately address new challenges in the coming year. "They should expect a moving landscape in lender acceptance and in cost of credit. Nothing dramatic expected here, but there will be changes nonetheless. Product evolution via expansion and adaptation will move at a moderate pace. F&I product evolution by providers trying to set their

products apart from the masses and adaptation to an emerging retail landscape will be present but not as high-powered and visible as I expect technology to be. Technology will be the F&I headliner for 2018.”

“Econtracting will continue its steady climb in overall usage as more and more dealers move forward to emenus and consumer ease of contracting,” said Mackie Hughes, president of the glass coat division for Simoniz. His thoughts were echoed by Performance Admin’s Knight, who appeared encouraged by dealers’ ability and willingness to adopt new ideas.

“Each year, dealers continue to embrace new technologies and automation in the F&I office. The processing of the deal, econtracting and API integration among the various product providers and banks will continue to evolve,” Knight said. “The forward-thinking providers will incorporate ‘Big Data’ and the utilization of machine learning to help F&I offices with predictive selling platforms to better counsel customers’ product selections.”

Portfolio’s Griggs expects vehicle manufacturers to continue to “ratchet up” their attempts to compete with F&I product providers. He also expects a small increase in online vehicle sales, “which will have a negligible impact on independent F&I providers in 2018 but which will require new business models for us to remain relevant in the long term. I also believe autonomous vehicles and all electric vehicles will have zero impact on the F&I business in 2018 despite some people’s belief that these trends are ‘upon us.’”

“Digital retail is in the bottom of the first inning and runners are on base, which means there is no need to panic but also don’t let the game get away from you too quickly,” said Safe-Guard’s Duncan. “One dealer told me, ‘I won’t be first, but I will be second.’ That’s sage advice.” Duncan said he would advise dealers to share more information about F&I products online to establish themselves as a resource for customers while improving their search-engine returns. He recommends “filling that space with very simple, benefit-oriented content for consumers who are searching inventory on your site, and Googling protection products — e.g. ‘What is GAP protection?’ — in your area. If a customer comes into the finance office and is aware of and interested in the products before you get into the menu, that’s a win.”

John Pappanastos, president and CEO of EFG Companies, said manufacturers learned a “big lesson” in 2017 that will affect their fleets going forward.

“Today’s consumers want SUVs and CUVs,” Pappanastos said, and he expects dealers to increase their focus on F&I operations to secure upfront profits and retain more service customers. “The trend of rising vehicle prices will only continue, and dealers are expecting manufacturer incentives to dive even deeper, and are preparing to operate in another year with strained front-end margins. ... In their efforts to maximize back-end profitability, more dealers will look into retooling their product menus and F&I pay plans based on products that encourage consumers to return for service.”

**In addition to remaining focused on lending standards and lease metrics, Craig Robinson said he will keep a wary eye on providers who are focused on short-term gains at the expense of long-term viability.**

**“Specifically, within F&I, we will closely monitor various insurers’ approach to pricing. There are several carriers that currently offer woefully inadequate and almost irresponsible reserves,” said Robinson, the recently hired president of AAGI. “While this may allow certain product providers the ability to capture market share, it will undoubtedly result in either shock loss rate increases or full exit from the business at some point in the future. At AAGI, we are fiscally conservative and have no interest in joining the race to the bottom.”**

## **F&I Products**

Asked which F&I products will be big sellers in 2018, NAE/NWAN CEO Kelly Price answered, “Any product that helps a dealer build loyalty with a consumer. The push for online transactions has the potential to dramatically impact the traditional buying process. Any product that helps a dealership connect with the consumer on a personal level is critical to retaining repeat customers.”

CSO’s Wanning concurred, emphasizing the need to sell F&I products that drive repeat business. He expressed excitement about diminished asset protection (or “DAP”), also known as diminished value protection (DVP). He says DAP was designed to boost customer loyalty, increase dealers’ used-car inventories, and protect car buyers whose assets are badly damaged but not totaled.

“DAP is a great compliment to GAP. Whereas GAP provides a benefit if a car is totaled, DAP provides protection if a car is in an accident. The consumer can trade in their car back to the originating dealer — or any of the dealer’s other commonly owned dealerships — and receive a credit on the purchase or lease of another vehicle,” said Wanning, bringing the conversation back to the high loss ratios suffered by GAP providers and the concurrent hike in pricing.

“For the last couple of years, GAP has experienced an escalation in frequency and severity, which has resulted in increased pricing for many of the GAP products on the market. Even though GAP will continue to be a prominent offering on the menu, it is likely that there will be a larger emphasis on other automotive protection products and new offerings in the near future,” said Matt Croak, president of Wise F&I.

Though relatively new to the market, Croak added, DAP/DVP has been “widely accepted” by those dealers who have added the product to their menus. “Products that bring the customer back to the dealership — resulting in additional touchpoints — will assist dealers in fostering relationships and long-term loyalty with their customers.”

National Auto Care CEO Tony Wanderon believes consumers’ interest in protection products is at “an all-time high” and the industry is in a strong position heading into 2018. “I really think that the refinance sector will have a big jump once upside-down consumers shop for a new car and they cannot afford the payment. Refinancing provides the opportunity for them to lower their payment and possibly increase their credit score.”

“As leasing becomes more popular across the country, more lease-specific products, such as lease wear-and-tear, will become more popular,” added Max Zanan, president of Total Dealer Compliance and author of the recently released “Perfect Dealership: Surviving the Digital Disruption.”

AGWS's Lievrouw said the "core products" of vehicle service contracts and GAP — despite its recent troubles — will remain at the top of most dealers' menus in 2018. "With the extended finance terms we are seeing, there is a definite need for both of these products. The longer the finance term, the easier it should be to make a sale on both of these products, as the need is there for the consumer."

"F&I products will continue to be a driving force in overall dealer profits," said Simoniz's Hughes. "Ancillary products that are nonchargebackable will lead the way as well as more emphasis on service contracts and programs that drive the consumer back to the dealer service drive."

"Going into a second year of flat unit sales, dealers will be looking to agents for more solutions on how to maximize their back-end profit while also generating repeat business," said EFG's Pappanastos, citing NADA data showing that 83% of car buyers who remain in their selling dealer's service lanes will buy another vehicle from that dealer. "Keeping this in mind, I believe vehicle service contracts and other service retention-type products, like maintenance and CPO programs, will be the top sellers."

For US Equity's Steenbergh, however, the retention component will come second to a "positive customer experience."

"My reasoning? All of the disruptive models function to commoditize the auto sale. With no perceived benefit for the seller of the vehicle, it becomes a race to the bottom, looking for nothing but the lowest price," Steenbergh said. "The personal relationship with the dealer is gone. Couple that with the fact that it's far more cost-efficient to sell to a repeat customer than acquire a new one, and retention becomes the easiest way to combat decreasing sales margins."

To distinguish themselves from the "faceless sellers" with whom they compete, Steenbergh advises dealers to focus on "high-touch" service and an emphasis on customer relationship management. "Any F&I product that addresses those two issues should be a big seller."

### **Processes and Technology**

Rob Glander, president and CEO of GWC Warranty, described the growing adoption of electronic contracting and remittance — among franchised as well as independent dealers — as "staggering," noting that "All dealers are becoming very tech-savvy. From a VSC perspective, it's often about integrations with popular DMS providers."

As for the consumer-facing side of F&I technology, Duncan said, "Some people feel the menu is stale. Some even say the customer has 'figured it out.' I think that is a good thing. Customers don't want tricks. They want transparency, and the menu, when used properly, provides an honest and open conversation between the customer and the F&I manager. Isn't that the goal?"

Lievrouw expects a continued "slow" adoption of tablet-based presentations in 2018, which he believes will allow for a smoother transition from sales to F&I. "I believe this same technology can then be used to help power the online presentation to a consumer who is building their deal while sitting on their couch in their home," he said.

StoneEagle's Allen said she sensed a growing appreciation for the hybrid sales/F&I manager approach as well as predictive analytics, which could give agents and dealers new insights into F&I production.

"It is an exciting evolution, although the basic concept has been around and used for several years. But we see some issues with this approach. Current standards for most dealer groups is to show all products every time to reduce legal risk," Allen said. "Mark Virag and other industry experts have recently pointed out that, as you continue to use predictive processes, over time, it begins to skew the overall accuracy of the predictions themselves. So you end up having to show all the products again to make sure you get a continuous non-bias input of data. There are several ways to mitigate the potential issues and we think there will be continuous enhancement to this concept.

Zanan expressed curiosity over whether more dealer principals will adopt digital retailing of F&I products. "Currently it is very difficult for the consumer to obtain any information about F&I products that a particular dealership offers because F&I is one of the last remaining profit centers," he said. "Dealers are afraid of gross profit reduction if they provide or sell these products online."

"Millennials continue to impact the buying process and push toward a fully online transaction," said NAE/NWAN's Price. "One source close to us cited that, in a recent consumer survey, 75% of those surveyed indicated they would like to complete the entire purchasing process online. Buying services continue to pop up and are making it easier to find and purchase a car before walking into a dealership."

"Technology is constantly advancing, adoption continues to increase, and it will continue to do so in 2018 and beyond," said Wise F&I's Croak, who described the F&I industry as "somewhat behind the times relative to technology in the past," noting that other industries were quicker to adopt electronic business origination, for example. "However, for the past few years, we have been making up ground quickly and have experienced large increases in econtracting and online resources. F&I Express and other technology companies have done wonders for moving dealers to electronic origination by making connectivity easy."

Classic/Norman's Holcomb said she expects the shift toward econtracting to continue in 2018.

"Those that have held out are now realizing that with states constantly changing their required language dealers are having to update forms on a regular basis," she said. "Dealers also realize that it helps with compliance and eliminates pricing mistakes."

"On the technology and process front, it's going to be an exciting year and one where the consumer will continue to vote very strongly with their purchase behavior," said Allstate's Krasavage, noting that increased consumer expectations for "simplicity, transparency and speed" will drive the adoption of advanced F&I technology. "In order to best meet these expectations, there will no doubt be some continued redefinition of exactly what the 'F&I office' actually is within the car-buying experience. ... I think we'll see more dealers providing F&I product information, monthly payments that include F&I products, and even 'click to purchase' capabilities for F&I products directly on the dealer website."

## **Rules and Regulations**



No discussion of F&I's future would be complete without some concern over compliance issues. Describing the regulatory environment as "hard to forecast," GWC's Glander said he wouldn't have predicted many of the political and regulatory changes the nation has undergone since the end of 2016.

"I will say, however, that over many years in the auto industry, I have been consistently impressed with the commitment by dealers to doing the right things for their customers," Glander said. "I'm confident that the more people understand the critical role dealers play in helping people meet their transportation needs, the less they will feel a need for overregulation."

Much of our experts' discussion revolved around an unexpected and rather rocky changing of the guard at the federal Consumer Financial Protection Bureau. In November, former CFPB director Richard Cordray resigned and appointed one of his subordinates, Leandra English, to deputy director to ensure she would succeed him. But President Donald Trump had other ideas. He appointed his own interim director, Mick Mulvaney, a man who once described the agency as a "sad, sick joke." A federal judge ultimately sided with Trump, agreeing that the Federal Vacancies Reform Act allows the president to appoint whomever he wishes to the post.

**"I think everyone is interested to see what's going to happen with the CFPB. While I don't expect there to be any significant changes in 2018, it would be great to see a softened stance as it pertains to our industry," said AAGI's Robinson. "In addition, in Illinois, we expect revisions to the administrative code to allow all dealers the ability to offer their vehicles for sale with limited warranties included. This issue has impacted the industry as a whole, and I've taken it as a personal mission to lobby our state politicians to make the appropriate changes to the law."**

Given the outcome of the squabble over the director's chair, Allen said, "the automotive industry would like to see the agency establish a holistic approach involving a full view of consumer credit scores, vehicle characteristics and the structure, timing and location of each deal individually. Our industry may see some relief from the regulatory burdens of rate caps and product markup limits that have been building due to a more limited methodology that has been used by the CFPB."

Mick Mulvaney's appointment marked a "sharp reversal" of previous CFPB policy, Lindsey said. "With Republicans still controlling both the House and the Senate, further changes to the CFPB could be in the future, including giving Congress authority over its budget. It's still too early to tell, though, what will become of the CFPB in 2018. It likely wouldn't be dismantled, but its power could be drastically restricted."

"I see a significant change in consumer regulation of our products as the Trump administration reigns in the CFPB and their irrational approach to 'protecting' consumers," said Griggs. "However, all F&I providers need to continually demonstrate the value-added nature of our products and services and price them affordably. I expect an increase in state regulation of our products even as federal regulation eases."

Pappanastos said the automotive industry enjoyed "significant compliance wins" in 2017 and expressed hope for a redesigned CFPB.

“Now, for every new regulation the CFPB puts out, it must eliminate two. In addition, the CFPB’s arbitration rule was struck down by President Trump in the third quarter of 2017. Because of this, we don’t expect to see many new regulations come out from the bureau,” Pappanastos said. “However, the CFPB remains very fluid and should be watched. With these wins for the industry, dealers can be tempted to relax their compliance initiatives.”

The Federal Trade Commission, which, unlike the CFPB, has direct jurisdiction over auto dealers, “is still moving forward,” Pappanastos cautioned.

“In addition, consumer advocacy groups are still paying close attention to the industry. Remember, there are multiple ways our industry is regulated,” he said. “A great example of this is the cases I referenced earlier that are moving through lower courts now. One side effect of dealers owning their own data is how that data will be regulated under the Safeguards Rule. Dealer compliance policies for securing digital versions of nonpublic consumer data will come under greater scrutiny.”

“The only prediction about the regulatory environment that can be made with any confidence is that there will be change,” Krasavage said, noting that he does not anticipate any “sweeping” changes in 2018. However, “We have seen a larger number of bills associated with F&I product regulations being introduced and passed over the last several years,” he added, noting that most have brought minor changes to existing statutes and many have been supported by industry trade groups. “The departure of Richard Cordray and recent actions such as the CFPB arbitration rule being overturned could be harbingers of future changes in the complexion and focus of this agency.”

“Regulatory issues and compliance will continue to be a hot button, as will ridesharing and how that needs to be addressed from a service contract, GAP or other program coverages,” Hughes said. “I’m also interested in the CFPB and what the new appointee will do to their current role in all things dealer-related.”

Brown agreed, noting, “Regulatory pressures will come, it’s just a matter of when. Despite the changes at the CFPB, pressures on our industry will continue, whether it’s at a federal or state level, as evidenced by the October 2017 report from the National Consumer Law Center.”

“Rather than mention the agency that everyone else will, I’ll just say that the trends in this area are positive as we close out 2017 and I think will continue to be in 2018,” Atkinson said. He believes the F&I industry can continue to be profitable even as it advocates and demonstrates the need for a more transparent process. “With our current approach, we sell only about 35% to 40% of customers a service contract at the point of sale, for example. Let’s embrace the presentation in a straightforward way and see that number rise dramatically.”

As an example, Atkinson said he has seen VSC penetrations exceeding 60% in stores that offer a lifetime warranty and extoll its benefits throughout the marketing and sales processes.

“Customers buying vehicles with 90,000 miles and more say their greatest concern is whether the car will be reliable or not. They want VSC protection,” he said. “My point is, let’s be more transparent, offer the coverage to every customer every time, and you’ll see your F&I sales rise dramatically.”

## The Subscription Economy

A lengthy commitment to a vehicle, the financing that delivers it, and the protection products that protect it underpin F&I production. If the subscription economy becomes the new normal, will agents and dealers suffer?

"I'm not sure, but most customers don't buy their vehicles and own them a month at a time, so I believe protecting their vehicle for their estimated time of ownership is still the best value," Dorfman said. "Considering most of the benefits are cancelable, they can always pay for only what they've needed by canceling if they trade the vehicle in."

Wanderon agreed, noting that, "From my standpoint, F&I has always been a hybrid subscription. Think about it: Over 90% of products that are sold to consumers are funded by a lender and paid for over the term of the loan. Many, if not all, are cancelable at any time. That said, the only difference to me seems to be one is paid at a higher credit card rate and one is included in your monthly payment."

**"That's the million-dollar question. No one can deny the subscription economy is here to stay and will see continued adoption, particularly by the younger consumers," Robinson said. "I do not believe this will have a material impact on the F&I industry's production in 2018; however, all providers need to be planning mid- to long-term or run the risk of finding themselves passed by competitors. Furthermore, I expect the subscription economy to be most impactful in cities with significantly slower and dramatically less adoption in the suburbs and rural areas."**

Griggs sees "no appreciable impact" of the subscription economy on consumer purchasing habits in 2018. "In five years, however, the trends toward consumers purchasing discrete services rather than owning high maintenance products will inevitably begin to reduce demand for automobiles and, consequently, the demand for F&I products."

Steenbergh countered by pointing to the advent of monthly service contracts and the financing of F&I products beyond the finance term as evidence that the subscription economy is already affecting the industry.

"The vast majority of Americans are already conditioned payment buyers who live paycheck to paycheck," he said. "Fewer than 40% check their credit score. Consumer debt has returned to near-record highs. These people aren't focused on the long term as long as they can make the monthly payment and get what they want."

Crisorio described the subscription economy as "experimental," noting that the auto industry has already begun toying with the model at the factory level and beyond.

"There are many named programs out there, such as the technology platform Clutch or Canvas or Passport, and each promotes subscribing being easier than owning and more flexible than leasing," Crisorio said. "Consumer acceptance remains a question as to scale, as these programs are not for everyone. They can be pricey at \$300 to \$3,000 monthly, but simple in that they provide insurance, maintenance and roadside service plus pickup and delivery of the vehicle selected within a price band."

So if scale is a question, then so is success as an important business model. It could grow in importance, morph into another model, or just be a piece of the market.”

As for the year ahead, Crisorio added, “My Magic 8-Ball says it’s a piece of the retail market with a lot of onlookers. Stay tuned.”

“In 2018? Not much,” Lindsey said. “In years to come, possibly a substantial impact. If subscription services prove to be a viable long-term strategy for auto manufacturers, it has the possibility of impacting new-car sales and F&I product sales. Right now, it feels like there are more questions than answers.”

Noting that the cost for Ford’s vehicle-subscription service, Canvas, includes maintenance and a Ford- or Lincoln-branded service contract, Lindsey wondered whether OEMs would be compelled to require their dealers to limit their F&I offerings to factory-owned products for subscription units.

“If so, it could drastically limit the profitability of F&I product sales,” he said. “Separately, there are a handful of Silicon Valley startups with subscription-based models that could cause a disruption in the auto industry. What effect they would have on the way consumers purchase F&I products is still unknown, but, if it’s successful, it could create a consolidation of F&I product providers.”

Pruitt was unequivocal about the effect of the subscription economy on F&I production.

“OEM subscription models will likely negatively impact F&I sales and thus dealers’ bottom lines,” he said. “For decades, the dealers and the F&I industry have significantly relied on the live, one-on-one presentations made by the F&I professionals to maximize PVR profits. The skill level of these professionals simply cannot be duplicated in the subscription environment.”

“As I thought about this question, I thought about how active I am in the subscription economy,” Atkinson said. “Let’s see: Netflix, Amazon Prime, Spotify, Pandora, and the list grows rather quickly. In one sense, we have a subscription in that our products are typically tied into a loan and a monthly payment. Where I see great opportunity is in the 60% or so sales we miss and how to capitalize on them. I think that, over the next few years, you will see offerings that utilize a subscription model effectively realizing it is more than just a monthly payment. It needs to engage the customer and have a strong CRM component as well.”

Noting that the business model for buying cars continues to transform, Croak said, “Online research has turned into online purchasing, and this is no small change for the industry. Overall, I think the dealers are trying to see how best to support the customer through these shifts in buying. We all have to be willing to charter new territory when it comes to serving consumers and the role technology plays in the buying process.”

For his part, Zanan believes it may actually be easier to package F&I products in the subscription model. “There will be different plans, similar to how AT&T and Verizon price their cellphone plans,” he said.

“While there is a lot of activity in this space, where it will all settle out is far from clear,” Krasavage said. “I think that, over the next five years, we’ll see growth in subscription-type services over a number of

verticals — including automotive — some of which may not be so obvious.” In the short term, he added, “we are going to see a lot of experimentation and trial. From a product provider perspective, we will be flexible and adapt as we see market opportunities and needs arise. The strength of our brand, product portfolio and expertise will be solid assets for us wherever this leads. In the future, we may see areas where we can better deliver our existing F&I products to consumers following a subscription-type model in order to reduce purchase barriers and increase convenience for consumers.”

The key to success? Flexibility and anticipation. “Why are consumers interested in a subscription service? To save money? Reduce upfront costs? Flexibility?” Krasavage asked. “Understanding their needs and motivations will be key to determining the right areas to focus on.”

### **Bold Predictions**

Finally, we asked our experts if they cared to predict any major changes for 2018. Most pointed to external forces, including Wanning, who expressed further concerns about factory-branded F&I products.

“One of the trends I think could evolve is the OEMs’ development of providing a broader protection package for their vehicles,” he said. “Volkswagen recently came out with a six-year, 72,000-mile bumper-to-bumper transferrable warranty. If the VW program is a success, it could be copied by other OEMs and thereby reduce the ability of dealers to offer these products, which are crucial for F&I income.”

Weather was a major factor in 2017, Price said, and the effects will continue to be felt in the new year.

“We saw a spike in vehicle sales in the last quarter of 2017 due largely from the hurricanes that hit Texas and Florida. I believe we will continue to see this lift through the first quarter of 2018, but this is only temporary,” she said. “The market has plateaued, and manufacturers are looking outside of the United States for growth. It will be interesting to see how the global push from major automakers will impact the U.S. market.”

Bringing the conversation back around to GAP losses, Holcomb said there is “a lot of talk” about fitting the cornerstone product into the F&I landscape in 2018. “I think there will still continue to be price increases as administrators grapple with the best way to keep the program profitable for everyone, and yet I think there will be a shift at some point away from the simple three-tier approach to something more dynamic that fits the marketplace,” she said.

“Short of some catastrophic event tanking business and consumer confidence — like a missile exchange with North Korea — I don’t see any major changes,” Steenbergh said. “For better or worse, our economy is heavily driven by emotion.”

Zanan concurred, noting that “Change happens slowly and incrementally, so nothing drastic should happen in 2018. Consumers will continue to engage in more digital retail, and that will put pressure on car dealers to adopt to these changing consumer shopping trends.”

“While it is important to pay attention to longer-term trends impacting the automotive industry and prepare for them, there is no reason for F&I providers to panic about the near future,” Griggs said. “Successful F&I providers that focus on creating wealth for their dealer clients through income development and great service will continue to fare well.”

Several of our experts said dealers will look to shore up internal processes to drive profits. Knight, for example, expects dealers to continue to look for new ways to grow sales and service revenue with less reliance on “traditional and expensive” advertising methods. Pappanastos said pre-owned inventories are “rightsized” going into 2018, so he expects dealers to put a premium on sourcing trade-in and off-lease units at the expense of the auctions.

Of course, there is no F&I without sales, and Glander expressed some concern over the shrinking subprime auto finance market.

“Last year, we saw a number of the largest banks and lenders pull back from the auto lending space, particularly with riskier loans. I think it’s worth really understanding the drivers of those moves, which in some cases appear to be an effort to repair image issues at the banks and heal self-inflicted wounds,” Glander said. “We believe that the auto consumer lending business remains an opportunity for finance companies to earn tremendous returns while serving consumers and a dealer industry that is critical to the economy. If the past is any indication, we will see a number of smaller lenders step in to fill the hole left by the big players.”

“I see continued dealer consolidation,” Duncan said. “This is not a bold prediction, but I believe one of the biggest stories of the year will be about the merger of two of the publicly traded dealer groups. I have no sense of who these participants may be, but we have yet to see a merger of this proportion. Lithia and DCH would be the closest example of two auto dealer juggernauts combining as one company. Name another industry where there has never been a merger of two Top Five market-share leaders.”

“Consolidation in all areas, I think, will be in play,” Wanderson said. “Agencies, administrators, underwriters and dealers will get bigger and bigger. Seems to me if you are not getting bigger in 2018, you are going to be in trouble.”